

Regulatory Rout: China's stock market amidst recent crackdown

DIGITAL ENGAGEMENT TEAM

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TRADING MATTERS SERIES: NEWS FOCUS

The summary and impact of a major news event

The latest on the recent China regulatory crackdown:

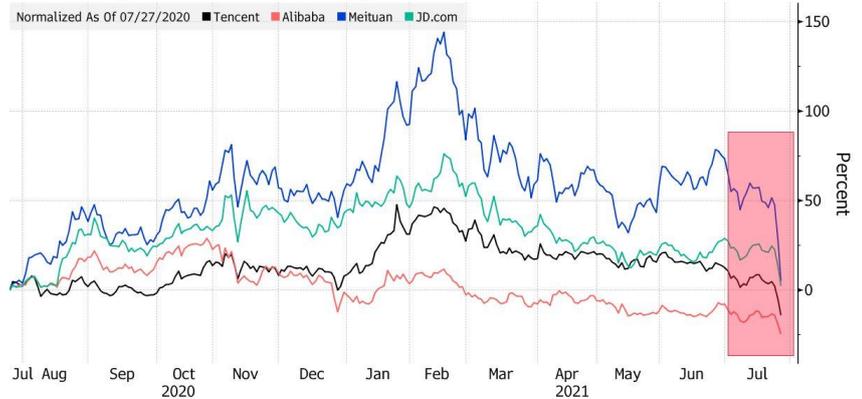
What happened?

Since November 2020, Beijing has embarked on an unprecedented regulatory clampdown.¹ Starting with the last-minute scuttling of Ant Group's IPO, the crackdown began with China's Big Tech firms¹ but in recent weeks have extended well beyond to sectors from private education to digital gaming, e-cigarettes and property.²

The US\$1 trillion selloff as Beijing tightens its grip has triggered a new round of soul searching amongst investors about the case for Chinese assets, amid the wild market swings and volatility.^{3,5}

No One Spared

China's largest internet suffer heavy selloff amid crackdown



What's the crackdown all about? And why?

Previously in the 1980s, Deng Xiaoping set the tone when he said it was OK if some got rich first.⁴ Now amid a climate of slowing growth and increasingly hostile relations with the US, China's policy has since shifted to prioritizing social stability, common prosperity and national security ahead of unfettered economic growth.^{4,18} The government's moves to go after industries that create the most social discontent also comes ahead of the once-in-a-decade leadership transition next year, where Chinese leader Xi Jinping is expected to buck tradition and stay on as party chief.⁴

The recent crackdown can be broadly categorized into three different areas, happening simultaneously:¹



Antitrust

Antitrust scrutiny is not something unique to China,^{1,6} but has hit Chinese companies across a wide range of sectors.¹ In April 2021, Alibaba became the largest victim thus far of China's antitrust probe when it was fined a record US\$2.8 billion.¹ 33 other tech firms were also called in by regulators to rectify antitrust practices.^{1,7}



Data Security

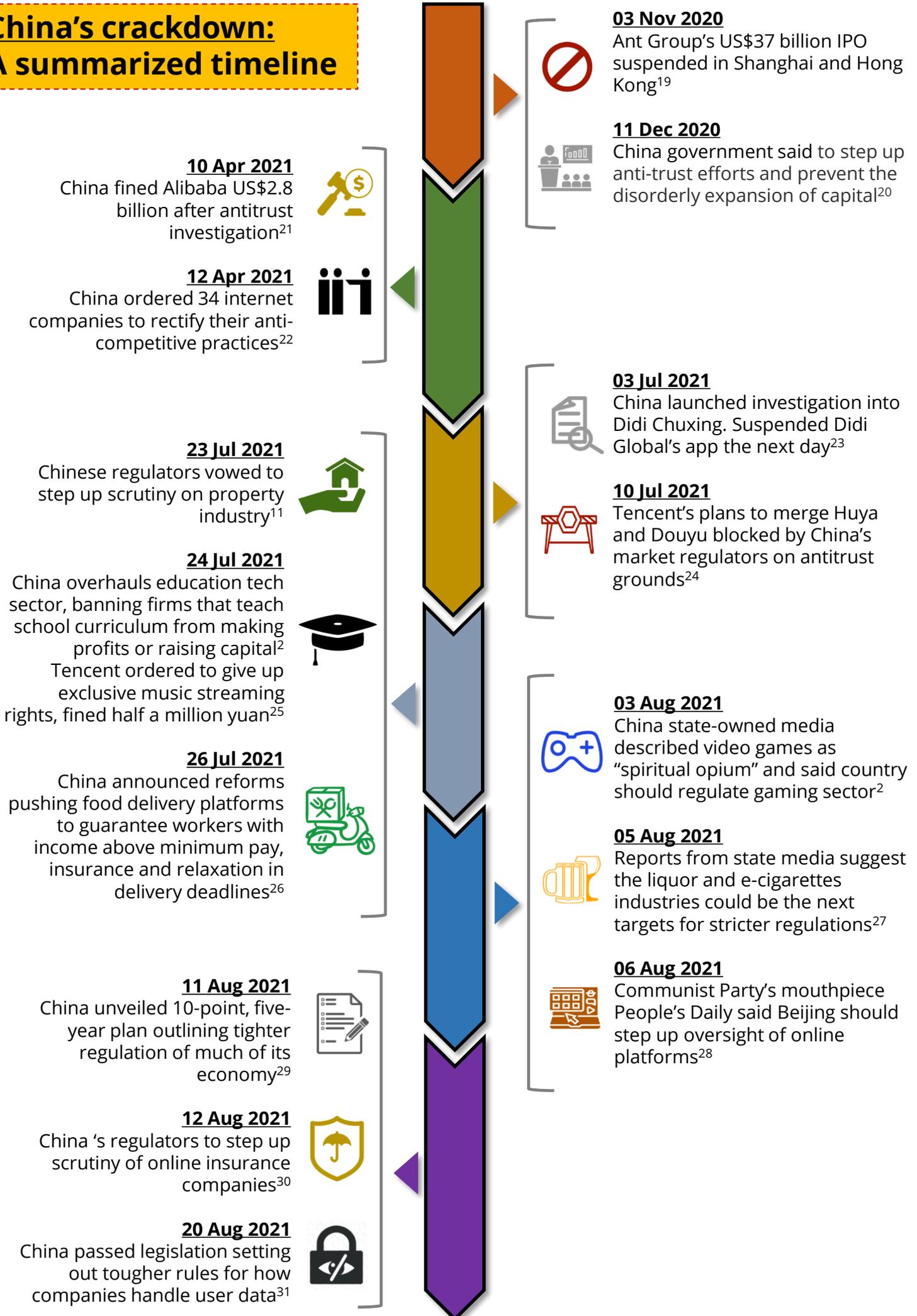
US-listed Didi has been the biggest victim of data security enforcement thus far, after its app got suspended for violating data security protocols two days after its IPO in the US.¹ China's regulators are worried about data being leaked to foreign adversaries, or that the U.S. might gain some leverage on U.S.-listed Chinese companies.¹



Not in Public Interest

The catch-all phrase "disorderly expansion of capital" may be interpreted as "growth at the expense of the public interest", and was emphasized during the Politburo's meeting in December 2020.^{1,8} Efforts to prevent this may help explain crackdowns on Ant Group's IPO, ByteDance and Tencent, and most recently the education and tutoring sector.¹

China's crackdown: A summarized timeline



How does this affect the financial markets?

What are some of the hardest hit sectors from this regulatory crackdown?



Education

Beijing recently unveiled a sweeping overhaul of its US\$100 billion education tech sector, banning companies that teach the school curriculum from making profits, raising capital or going public.^{2,9} Stemming from backlash against the industry as excessive tutoring and high fees exacerbates inequalities in society,⁹ record losses for education stocks swiftly followed, with several diving up to 70% in a single trading session.^{2,9}



Tech

China's Big Tech firms and their sizable market power¹⁰ have been brought to heel in the recent crackdown. From Alibaba's record antitrust fine,¹⁰ to new guidelines on food platforms such as Meituan,² the tech sector faces some of the harshest measures from Beijing to date.¹⁰ As companies adapt, some are even eager to preempt authorities and "self-correct", imposing restrictions on or their own businesses.¹⁰



Property

Xi Jinping famously said "housing is for living in and not for speculation".¹¹ Previously already under scrutiny for years, Beijing has intensified its focus on real estate by raising mortgage rates and tightening policy as it cracks down on businesses seen as widening social inequities.¹² China has also vowed to "notably improve order" in the market and regulate a wide range of activities across property management.¹¹



Liquor/E-Cigarettes

A series of reports from state media on liquor and e-cigarette stocks has some investors skittish that this could potentially foreshadow the next targets for stricter regulation.² A vaping crackdown threatens to snuff out the industry with plans of expanded regulations and tax hikes by 400%,¹⁴ while it was reported distillers will meet regulators over market order.¹³

Market Talk: What else is being said about the ongoing crackdown? Will it continue?

According to some analysts, this signals the beginning of a new era, as the government puts socialism before shareholders and regulatory changes rip apart the old playbook.¹⁸

Opinions are mixed. Some investors have decided China just isn't worth the trouble, while others spot buying opportunities after valuations sank to the lowest level in decades.³ Amid one of China's biggest economic policy shifts since the 1980s, signs are that the regulatory onslaught has further to run.^{3,6} A five-year blueprint calling for greater regulation provides a sweeping framework for the broader crackdown,¹⁷ and some believe the government is just getting started in its push to realign the relationship between private business and the state.⁶

Breaking Point

KWEB snaps inflow streak as losses pile up



Source: Bloomberg

Several prominent investors such as Cathie Wood and SoftBank chief Masayoshi Son have publicly expressed their reservations about investing in China, dumping shares despite low valuations, or pulling back from investing in the country while waiting for more regulatory clarity.¹⁵ Yet funds such as the KraneShares CSI China Internet Fund (KWEB) saw five weeks of inflows and dip-buying, although that has reversed in recent days.¹⁶

Education

Below are the top companies based on Market Cap in their respective industries in China

New Oriental Education & Technology – ADR (EDU US)



- Largest provider of private educational services in China (PR Newswire)
- New Oriental Education have cancelled its upcoming earnings releases and media calls amid Beijing's intensified crackdown on off-campus tutoring (31 Jul 2021, SCMP)

Market Cap (USD)	3.10 Billion
Analysts' 12M Target Price	7.17
Current Price	1.81

TAL Education Group (TAL US)



- TAL Education announced that it will hold its annual general meeting of shareholders on 23 Aug 2021 (16 Aug 2021, PR Newswire)
- TAL Education have cancelled its upcoming earnings releases and media calls amid Beijing's intensified crackdown on off-campus tutoring (31 Jul 2021, SCMP)

Market Cap (USD)	3.27 Billion
Analysts' 12M Target Price	18.48
Current Price	5.07

Koolearn Technology (1797 HK)



- Koolearn expects that its compliance with the new regulatory measures would have a material impact on its existing Academic AST business but will not have a material impact on its other businesses, including college education and overseas test preparation services (19 Aug 2021, Aastocks)
- Koolearn announces a meeting of the Board to be held on 27 Aug 2021 (Koolearn)

Market Cap (USD)	519 Million
Analysts' 12M Target Price	14.34
Current Price	4.04

Gaotu Techedu (GOTU US)



- Gaotu Techedu announced on 17 Aug 2021 that Mr. Wei Liu, Vice President, has resigned due to personal reasons. The resignation is effective on the same day (17 Aug 2021, PR Newswire)
- Chen Xiangdong, founder and CEO of Gaotu Techedu, confirmed on 30 Jul 2021 that quite a few employees would be let go and said a large-scale adjustment of the organizational structure is inevitable (05 Aug 2021, Pandaily)

Market Cap (USD)	608 Million
Analysts' 12M Target Price	25.16
Current Price	2.38

Technology

Below are the top companies based on Market Cap in their respective industries in China

Tencent (700 HK)



- Tencent earmarks US\$7.7bn fund dedicated to “common prosperity”, one day after Chinese President Xi Jinping made it a key economic and social goal for the country (19 Aug 2021, SCMP)
- Tencent beat forecasts with a 29% jump in second-quarter profit. Net profit for the three months through June came in at 42.6billion yuan, revenue jumped 20% to 138.3billion yuan (18 Aug 2021, CNA)

Market Cap (USD)	524.16 Billion
Analysts' 12M Target Price	669.62
Current Price	425.4

Alibaba (9988 HK)



- Alibaba shares slumped as much as 5.4% to a record low in Hong Kong on 19 Aug 2021 after Beijing hit the industry with a fresh round of regulations (19 Aug 2021, Bloomberg)
- Alibaba launched its first NFT marketplace platform that lets musicians and artists sell the rights to their content via blockchain with the approval of the Sichuan government (19 Aug 2021, Investing.com)

Market Cap (USD)	440.70 Billion
Analysts' 12M Target Price	268.54
Current Price	157.9

Meituan (3690 HK)



- Meituan is testing a social feature for food-ordering users as part of the company's effort to find new growth areas. The new feature allows users to share orders with their contacts on the Meituan app (13 Aug 2021, Technode)
- China's antitrust regulator is preparing to impose a roughly US\$1 billion fine on food-delivery giant Meituan for allegedly abusing its dominant market position to the detriment of merchants and rivals (06 Aug 2021, MarketWatch)

Market Cap (USD)	152.16 Billion
Analysts' 12M Target Price	359.58
Current Price	193.4

JD.COM (9618 HK)



- JD.com is on track to become China's first e-commerce player with its own air cargo fleet after the Civil Aviation Administration of China gave preliminary approval for the establishment of Jiangsu Jingdong Cargo Airlines (05 Aug 2021, SCMP)

Market Cap (USD)	96.61 Billion
Analysts' 12M Target Price	395.18
Current Price	241.4

Property Development/Property Services

Below are the top companies based on Market Cap in their respective industries in China

China Evergrande Group (3333 HK)



- Earnings announcement for period ending S1/2021: 31 Aug 2021 (Bloomberg)
- Evergrande Group said on 20 Aug 2021 it is determined to maintain the stability of its operations, a day after the indebted company were issued a rare warning by regulators that the company needed to reduce its debt risks and prioritise stability (20 Aug 2021, CNA)
- Xia Haijun, chief executive of China Evergrande, sold about HK\$115.6 million worth of stakes in the group's electric-car making unit and property management arm on 11 Aug 2021 (18 Aug 2021, SCMP)

Market Cap (USD)	8.37 Billion
Analysts' 12M Target Price	12.42
Current Price	4.92

China Vanke Group (2202 HK)



- Earnings announcement for period ending Q2/2021: 27 Aug 2021 (Bloomberg)
- China Vanke was rumored to be one of the potential buyer of Evergrande's assets, including stakes in its new-energy vehicle and property units last week. But mainland media reported later that both companies were no longer interested (20 Aug 2021, The Standard)

Market Cap (USD)	39.53 Billion
Analysts' 12M Target Price	33.68
Current Price	22.6

Country Garden Services (6098 HK)



- Earnings announcement for period ending S1/2021: 25 Aug 2021 (Bloomberg)
- Country Garden Holdings' property management arm is among several potential buyers for assets of Evergrande Property Services, Caixin reported on 10 Aug 2021. However, it was reported two days later that Country Garden were no longer interested (16 Aug 2021, Bloomberg)

Market Cap (USD)	22.35 Billion
Analysts' 12M Target Price	91.59
Current Price	53.95

China Resources Mixc Lifestyle Services (1209 HK)



- Earnings announcement for period ending S1/2021: 25 Aug 2021 (Bloomberg)
- Share price closed at HK\$41.05, 25.70% off its 2021 high of HK\$55.25 as at 19 Aug 2021 (19 Aug 2021, TradingView)

Market Cap (USD)	11.29 Billion
Analysts' 12M Target Price	53.88
Current Price	38.55

Liquor/E-Cigarettes

Below are the top companies based on Market Cap in their respective industries in China

Kweichow Moutai (600519 SH)



- Kweichow Moutai's net profit for the first half of the year grew 9.1% compared with the same period a year earlier to 24.65billion yuan as revenue rose 12% to 49.09billion yuan (01 Aug 2021, MarketWatch)

Market Cap (USD)	299.21 Billion
Analysts' 12M Target Price	2276.58
Current Price	1548

Wuliangye Yibin (ticker)



- Earnings announcement for period ending Q2/2021: 29 Aug 2021 (Bloomberg)
- The Central Commission for Discipline Inspection, the Chinese Communist party's anti-corruption watchdog, said pressure to drink could lead to crimes and such practices should be replaced with "correct values", according to a commentary on its website (11 Aug 2021, Financial Times)

Market Cap (USD)	123.26 Billion
Analysts' 12M Target Price	331.06
Current Price	206.38

Smooore International (6969 HK)



- Shares in RLX Technology and smaller peers Smooore International Holdings and China Boton Group Co tumbled after state news agency Xinhua published a report saying that minors were gaining easy access to e-cigarettes (05 Aug 2021, Reuters)

Market Cap (USD)	30.23 Billion
Analysts' 12M Target Price	76.39
Current Price	39.3

Relx Technology (RLX US)



- Xinhua News Agency, an official media of Chinese government, on 04 Aug 2021 issued a document highlighting the necessity to prohibit e-cigarettes from being used by minors (05 Aug 2021, Pandaily)

Market Cap (USD)	6.64 Billion
Analysts' 12M Target Price	19.04
Current Price	4.23

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